

DERRY TOWNSHIP POLICE PENSION PLAN

DAUPHIN COUNTY

COMPLIANCE AUDIT REPORT

FOR THE PERIOD

JANUARY 1, 2007, TO DECEMBER 31, 2009



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BACKGROUND

On December 18, 1984, the Pennsylvania Legislature adopted the Municipal Pension Plan Funding Standard and Recovery Act (P.L. 1005, No. 205, as amended, 53 P.S. § 895.101 et seq.). The act established mandatory actuarial reporting and funding requirements and a uniform basis for the distribution of state aid to Pennsylvania's public pension plans. Section 402(j) of Act 205 specifically requires the Auditor General, as deemed necessary, to make an audit of every municipality which receives general municipal pension system State aid and of every municipal pension plan and fund in which general municipal pension system State aid is deposited.

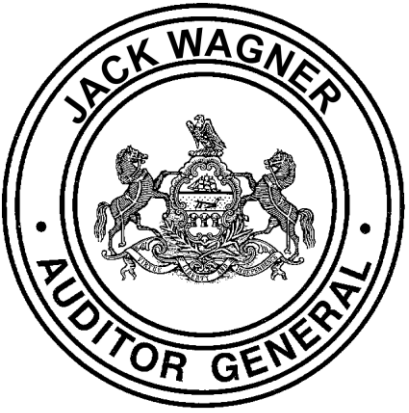
Pension plan aid is provided from a 2 percent foreign casualty insurance premium tax, a portion of the foreign fire insurance tax designated for paid firefighters and any investment income earned on the collection of these taxes. Generally, municipal pension plans established prior to December 18, 1984, are eligible for state aid. For municipal pension plans established after that date, the sponsoring municipality must fund the plan for three plan years before it becomes eligible for state aid. In accordance with Act 205, a municipality's annual state aid allocation cannot exceed its actual pension costs.

In addition to Act 205, the Derry Township Police Pension Plan is also governed by implementing regulations adopted by the Public Employee Retirement Commission published at Title 16, Part IV of the Pennsylvania Code and applicable provisions of various other state statutes including, but not limited to, the following:

Act 147 - Special Ad Hoc Municipal Police and Firefighter Postretirement Adjustment Act, Act of December 14, 1988 (P.L. 1192, No. 147), as amended, 53 P.S. § 896.101 et seq.

Act 600 - Police Pension Fund Act, Act of May 29, 1956 (P.L. 1804, No. 600), as amended, 53 P.S. § 761 et seq.

The Derry Township Police Pension Plan is a single-employer defined benefit pension plan locally controlled by the provisions of Ordinance No. 180, as amended, adopted pursuant to Act 600. The plan is also affected by the provisions of collective bargaining agreements between the township and its police officers.



Board of Township Supervisors
Derry Township
Dauphin County
Hershey, PA 17033

We have conducted a compliance audit of the Derry Township Police Pension Plan for the period January 1, 2007, to December 31, 2009. The audit was conducted pursuant to authority derived from Section 402(j) of Act 205 and in accordance with *Government Auditing Standards* applicable to performance audits issued by the Comptroller General of the United States. Those standards require that we plan and perform our audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

The objectives of the audit were:

1. To determine if municipal officials took appropriate corrective action to address the finding contained in our prior audit report; and
2. To determine if the pension plan was administered in compliance with applicable state laws, regulations, contracts, administrative procedures, and local ordinances and policies.

Our audit was limited to the areas related to the objectives identified above. Derry Township contracted with an independent certified public accounting firm for annual audits of its basic financial statements which are available at the township's offices. Those financial statements were not audited by us and, accordingly, we express no opinion or other form of assurance on them.

Township officials are responsible for establishing and maintaining effective internal controls to provide reasonable assurance that the Derry Township Police Pension Plan is administered in compliance with applicable state laws, regulations, contracts, administrative procedures, and local ordinances and policies. In conducting our audit, we obtained an understanding of the township's internal controls as they relate to the township's compliance with those requirements and that we considered to be significant within the context of our audit objectives, and assessed whether those significant controls were properly designed and implemented. Additionally, we tested transactions, assessed official actions, performed analytical procedures and interviewed selected officials to the extent necessary to satisfy the audit objectives.

The results of our tests indicated that, in all significant respects, the Derry Township Police Pension Plan was administered in compliance with applicable state laws, regulations, contracts, administrative procedures, and local ordinances and policies, except as noted in the following findings further discussed later in this report:

Finding No. 1 – Noncompliance With Prior Audit Recommendation – Pension Benefits Not In Compliance With Act 600 Provisions

Finding No. 2 – In-Service Retirement Option Plan Not Adopted By Ordinance

The accompanying supplementary information is presented for purposes of additional analysis. We did not audit the information and, accordingly, express no form of assurance on it.

The contents of this report were discussed with officials of Derry Township and, where appropriate, their responses have been included in the report.

October 14, 2010

JACK WAGNER
Auditor General

DERRY TOWNSHIP POLICE PENSION PLAN
STATUS OF PRIOR FINDING

Noncompliance With Prior Audit Recommendation

Derry Township has not complied with the prior audit recommendation concerning the following as further discussed in the Findings and Recommendations section of this report:

- Pension Benefits Not In Compliance With Act 600 Provisions

DERRY TOWNSHIP POLICE PENSION PLAN
FINDINGS AND RECOMMENDATIONS

Finding No. 1 - Noncompliance With Prior Audit Recommendation - Pension Benefits Not In Compliance With Act 600 Provisions

Condition: As disclosed in the prior audit report, the township enacted Ordinance No. 551 to bring the pension plan’s benefit structure into compliance with Act 600, as amended. However, the pension plan’s governing document, Ordinance No. 180, as amended, fails to contain a benefit provision that is required by Act 600 as noted below:

| <u>Benefit Provision</u> | <u>Governing Document</u> | <u>Act 600 (as amended)</u> |
|-------------------------------------|---------------------------|--|
| Intervening military service credit | Not provided | Any member of the police force employed by a municipality for at least 6 months and who enters into military service of the United States shall have credited to his employment record for pension or retirement benefits all of the time spent in such military service, if such member returns to his employment within 6 months after his separation from military service. |

Criteria: A governing document which contains clearly defined and updated benefit provisions is a prerequisite for the consistent, sound administration of retirement benefits. In addition, the police pension plan’s benefit structure should be in compliance with Act 600, as amended.

Cause: Municipal officials failed to establish adequate internal control procedures to ensure compliance with the prior audit recommendation.

Effect: Maintaining a benefit structure which is not in compliance with Act 600 could result in plan members or their beneficiaries receiving incorrect benefit amounts or being denied benefits to which they are statutorily entitled.

Recommendation: We again recommend that municipal officials, after consulting with their solicitor, take whatever action is necessary to bring the police pension plan’s benefit structure into compliance with Act 600, as amended, at their earliest opportunity to do so.

Management’s Response: Municipal officials agreed with the finding without exception.

DERRY TOWNSHIP POLICE PENSION PLAN
FINDINGS AND RECOMMENDATIONS

Finding No. 2 – In-Service Retirement Option Plan Not Adopted By Ordinance

Condition: The terms, provisions and conditions of the In-Service Retirement Option Plan (IROP) were adopted in an addendum to the collective bargaining agreement between Derry Township and the Derry Township Police Association, dated February 27, 2007, effective January 1, 2007. However, the terms and conditions of the IROP have not been formally adopted by an ordinance that would properly amend the plan’s benefit structure.

Criteria: Section 1(a) of Act 600 states, in part:

Each borough, town and township of this Commonwealth maintaining a police force of three or more full-time members and each regional police department shall, and all other boroughs, towns or townships may, establish, by ordinance or resolution. . . .

Furthermore, In Wynne v. Lower Merion Township, 181 Pa. Superior Ct., 524, the Pennsylvania Superior Court held that an ordinance may be amended only by another ordinance and not by a resolution.

Cause: Plan officials were unaware of the need to formally adopt the provisions of the IROP through a properly executed ordinance.

Effect: The failure to include the IROP benefit provisions in the plan’s governing document could result in inconsistent or improper benefit calculations and incorrect benefit payments from the pension plan.

Recommendation: We recommend that municipal officials take appropriate action to formally adopt the IROP terms and conditions through a properly executed ordinance.

Management’s Response: Municipal officials agreed with the finding without exception.

DERRY TOWNSHIP POLICE PENSION PLAN
 SUPPLEMENTARY INFORMATION
 (UNAUDITED)

SCHEDULE OF FUNDING PROGRESS

Historical trend information about the plan is presented herewith as supplementary information. It is intended to help users assess the plan's funding status on a going-concern basis, assess progress made in accumulating assets to pay benefits when due, and make comparisons with other state and local government retirement systems.

The actuarial information is required by Act 205 biennially, except for distressed pension plans, for which annual reporting was required through January 1, 2003. The historical information, beginning as of January 1, 2005, is as follows:

| | (1) | (2) | (3) | (4) | (5) | (6) |
|--------------------------|-------------------------------|---|--|----------------------|---------------------|--|
| Actuarial Valuation Date | Actuarial Value of Assets (a) | Actuarial Accrued Liability (AAL) - Entry Age (b) | Unfunded (Assets in Excess of) Actuarial Accrued Liability (b) - (a) | Funded Ratio (a)/(b) | Covered Payroll (c) | Unfunded (Assets in Excess of) Actuarial Accrued Liability as a % of Payroll [(b-a)/(c)] |
| 01-01-05 | \$ 7,184,486 | \$ 9,275,861 | \$ 2,091,375 | 77.5% | \$ 2,449,307 | 85.4% |
| 01-01-07 | 8,357,457 | 10,968,100 | 2,610,643 | 76.2% | 2,601,960 | 100.3% |
| 01-01-09 | 9,502,245 | 12,795,727 | 3,293,482 | 74.3% | 2,798,837 | 117.7% |

Note: The market value of the plan's assets at 01-01-09 has been adjusted to reflect the smoothing of gains and/or losses over a 5-year averaging period, subject to a maximum of 130 percent and a minimum of 70 percent of market value. This method will lower contributions in years of less than expected returns and increase contributions in years of greater than expected returns. The net effect over long periods of time is to have less variance in contribution levels from year to year.

DERRY TOWNSHIP POLICE PENSION PLAN
SUPPLEMENTARY INFORMATION
(UNAUDITED)

The comparability of trend information is affected by changes in actuarial assumptions, benefit provisions, actuarial funding methods, accounting policies, and other changes. Those changes usually affect trends in contribution requirements and in ratios that use the actuarial accrued liability as a factor.

Analysis of the dollar amount of the actuarial value of assets, actuarial accrued liability, and unfunded (assets in excess of) actuarial accrued liability in isolation can be misleading. Expressing the actuarial value of assets as a percentage of the actuarial accrued liability (Column 4) provides one indication of the plan's funding status on a going-concern basis. Analysis of this percentage, over time, indicates whether the system is becoming financially stronger or weaker. Generally, the greater this percentage, the stronger the plan.

Trends in unfunded (assets in excess of) actuarial accrued liability and annual covered payroll are both affected by inflation. Expressing the unfunded (assets in excess of) actuarial accrued liability as a percentage of annual covered payroll (Column 6) approximately adjusts for the effects of inflation and aids analysis of the plan's progress made in accumulating sufficient assets to pay benefits when due. Generally, where there is an unfunded actuarial accrued liability, the smaller this percentage, the stronger the plan. However, when assets are in excess of the actuarial accrued liability, the higher the bracketed percentage, the stronger the plan.

DERRY TOWNSHIP POLICE PENSION PLAN
SUPPLEMENTARY INFORMATION
(UNAUDITED)

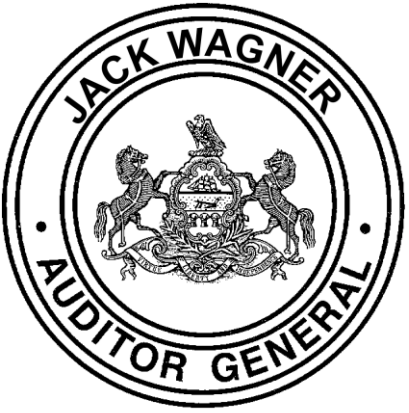
SCHEDULE OF CONTRIBUTIONS FROM EMPLOYER
AND OTHER CONTRIBUTING ENTITIES

| Year Ended December 31 | Annual Required Contribution | Percentage Contributed |
|------------------------|------------------------------|------------------------|
| 2004 | \$ 370,341 | 100.0% |
| 2005 | 556,745 | 100.0% |
| 2006 | 519,119 | 100.0% |
| 2007 | 486,362 | 103.3% |
| 2008 | 476,294 | 100.0% |
| 2009 | 625,158 | 100.0% |

DERRY TOWNSHIP POLICE PENSION PLAN
 SUPPLEMENTARY INFORMATION
 NOTES TO SUPPLEMENTARY SCHEDULES
 (UNAUDITED)

The information presented in the required supplementary schedules was determined as part of the actuarial valuation at the date indicated. Additional information as of the latest actuarial valuation date follows:

| | |
|-------------------------------|--|
| Actuarial valuation date | January 1, 2009 |
| Actuarial cost method | Entry age normal |
| Amortization method | Level dollar |
| Remaining amortization period | 13 years |
| Asset valuation method | 5-year smoothing subject to a maximum of 130% and a minimum of 70% of market value |
| Actuarial assumptions: | |
| Investment rate of return * | 7.5% |
| Projected salary increases * | 5.5% |
| * Includes inflation at | Not disclosed |
| Cost-of-living adjustments | None assumed |



DERRY TOWNSHIP POLICE PENSION PLAN
REPORT DISTRIBUTION LIST

This report was initially distributed to the following:

The Honorable Edward G. Rendell
Governor
Commonwealth of Pennsylvania

Derry Township Police Pension Plan
Dauphin County
600 Clearwater Road
Hershey, PA 17033

Mr. E. Christopher Abruzzo Chairman, Board of Township Supervisors

Mr. James N. Negley Chief Administrative Officer

Ms. Cheryl Lontz Manager of Payroll & Employee Benefits

This report is a matter of public record. Copies of this report may be obtained from the Pennsylvania Department of the Auditor General, Office of Communications, Room 318 Finance Building, Harrisburg, PA 17120. If you have any questions regarding this report or any other matter, you may contact the Department of the Auditor General by accessing our website at www.auditorgen.state.pa.us.